



16  
No.'s 286 and 291

U.S. - Supreme Court, U. S.

FILED

SEP 10 1945

CHARLES ELMER CRISLEY  
CLERK

IN THE  
**Supreme Court of the United States**  
*October Term, 1945*

**THE DENVER AND RIO GRANDE WESTERN RAILROAD  
COMPANY,**

*Petitioner,*

*vs.*

**RECONSTRUCTION FINANCE CORPORATION, ET AL.,**

*Respondents.*

[No. 286]

**GUY A. THOMPSON, TRUSTEE, MISSOURI PACIFIC RAILROAD  
COMPANY, DENTOR,**

*Petitioner,*

*vs.*

**RECONSTRUCTION FINANCE CORPORATION, ET AL.,**

*Respondents.*

[No. 291]

**BRIEF IN OPPOSITION TO PETITIONS  
FOR CERTIORARI**

**HAROLD JUDSON**

*Acting Solicitor General*

**W. MEADE FLETCHER, JR.,**

811 Vermont Avenue, N. W.,

Washington 25, D. C.

*For Reconstruction Finance Cor-  
poration*

**RATHBONE, PERRY, KELLEY &  
DRYE**

ALEXANDER M. LEWIS

70 Broadway, New York 4, N. Y.

*For Central Hanover Bank and  
Trust Company, Trustee, Rio  
Grande Western Railroad Company  
First Trust Mortgage*

**DAVIS POLK WARDWELL SUN-  
DERLAND & KIENDL**

JOHN W. DAVIS

ERWIN S. S. SUNDERLAND

JAMES L. HOMER

THOMAS O'G. FITZGIBSON

JUDSON C. MCLESTER, JR.

15 Broad Street

New York 5, N. Y.

*For Guaranty Trust Company of  
New York, Trustee, Rio Grande  
Western Railroad Company Con-  
solidated Mortgage*

**HUNTON, WILLIAMS, ANDER-  
SON, GAY & MOORE**

HENRY W. ANDERSON

GEORGE D. GIBSON

Electric Bldg., Richmond 12, Va.

*For Insurance Group Committee*

**STEWART & SHEARER**

W. A. W. STEWART

45 Wall Street

New York 5, N. Y.

*For United States Trust Company  
of New York, Trustee, Denver and  
Rio Grande Railroad Company Con-  
solidated Mortgage*

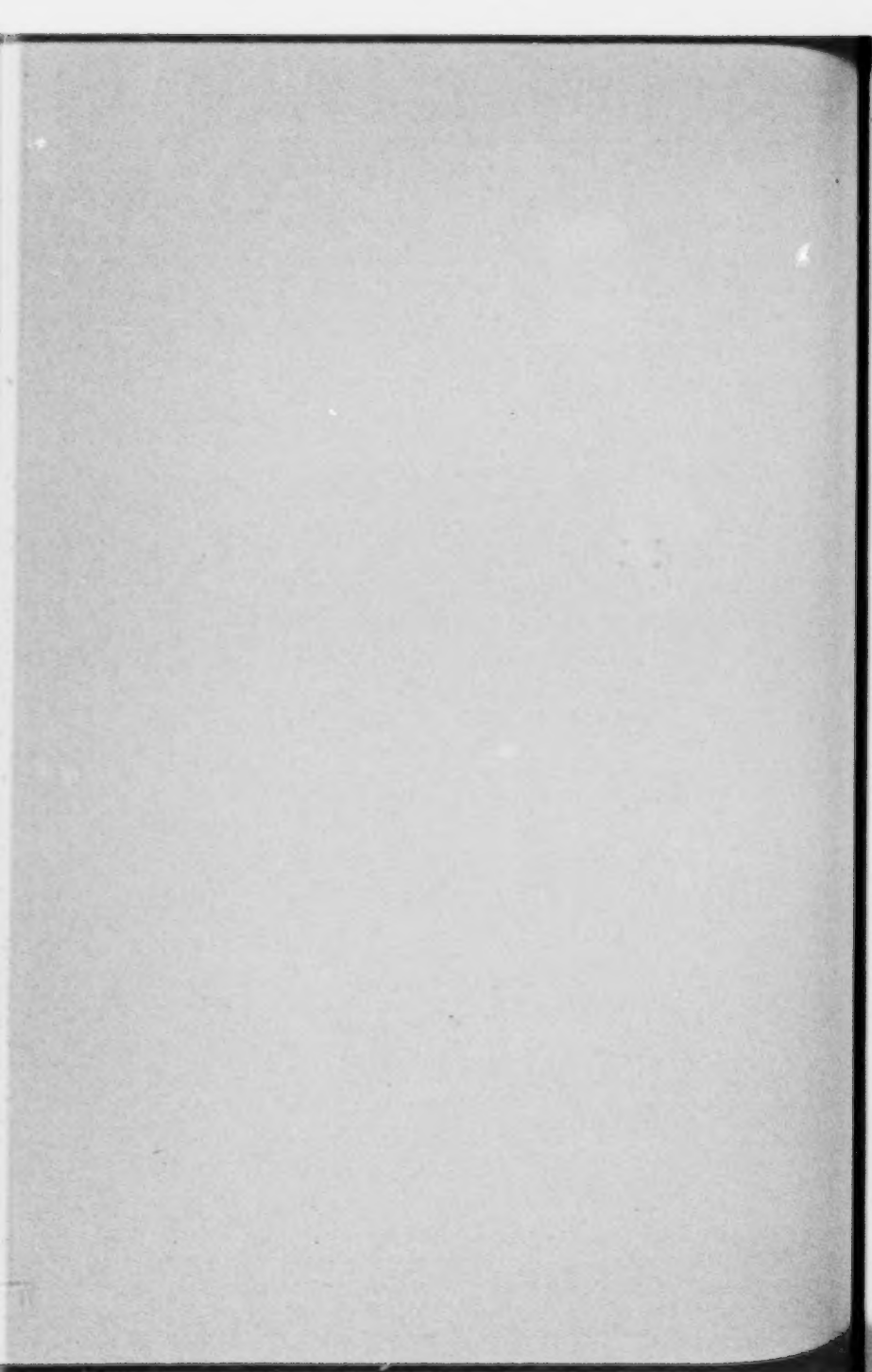
**MILBANK, TWEED & HOPE**

ARTHUR A. GAMMELL

15 Broad Street

New York 5, N. Y.

*For The Chase National Bank of  
the City of New York, Trustee, Den-  
ver and Rio Grande Western Rail-  
road Company Refunding and Im-  
provement Mortgage*



## BRIEF IN OPPOSITION TO PETITIONS FOR CERTIORARI

### A INTRODUCTORY STATEMENT

In the Denver and Rio Grande Western Railroad Reorganization two petitions for writs of certiorari have been filed in order to procure some allowance of new securities to the holders of the old stock. Of those petitions (the Stockholder Petitions) one is filed by The Denver and Rio Grande Western Railroad Company (the Debtor, No. 286) as a purported representative of the old preferred and common stock, the other by Guy A. Thompson, Trustee, Missouri Pacific Railroad Company (the Missouri Pacific, No. 291) as the holder of one-half of the old common stock. Though their reasoning differs, their aim is the same (recognition of the old stock) and they arise from the same reorganization, so both are answered in this one brief.

The parties to this brief are, or represent, holders of senior securities involved in the reorganization. Reconstruction Finance Corporation and Insurance Group Committee are large holders. The other parties hereto are indenture trustees under the senior mortgages.

While this reorganization involves a number of important questions that are of general concern and should be authoritatively resolved\*, it does not follow that all the other questions involved are of that character. On the contrary, other phases of the Commission's task below were, of course, merely an application to the facts in this reorganization of

---

\* See the Petition for writs of certiorari, dated July 31, 1945, that has been filed by the parties to this brief (No.'s 278-282, this Term). References herein to the record are to the record as filed in those cases, and the forms of reference are defined at p. *iv* of the Petition therein.

standards already settled by decisions of this Court. It is within that area that the Stockholder Petitions lie.

The Debtor's petition asserts that the whole philosophy of reorganization should now be re-written by this Court (Petition, pp. 3-9), but, failing that (on which we think no comment necessary), merely asks that a writ be granted to review the Circuit Court's approval of the exclusion of the old stock if, but only if, writs be granted in No.'s 278-282 to review the Circuit Court's disapproval of the Plan in other respects. No reasons are assigned for this request, except that the case, if brought here at all, may be brought "in its entirety" (p. 2). But that is a mistaken appeal. Resolution of the novel questions presented in No.'s 278-282 will in no way be impeded by the elimination, or aided by the inclusion, of the routine questions determining stockholder recognition. We think no further comment on the Debtor's Petition is needed.

The Missouri Pacific Petition does assign reasons for its request, but the questions to which they relate are, as indicated in the Argument below, not presented by the record.

## B ARGUMENT

Recognizing that the scope of the Commission's administrative functions in determining the permissible amount of the new capitalization has been settled by *Ecker v. Western Pacific R.*, 318 U. S. 448 (1943) and *Group of Institutional Investors v. Chicago, Milwaukee, St. Paul & Pacific R.*, 318 U. S. 523 (1943), the Missouri Pacific Petition seeks to show a reversible error of law within the meaning of those decisions by the assertion that the Commission was governed exclusively by the record of past earnings in times of depression, and gave no consideration to other factors.

But that is not true.

The Commission did not use as its decisive criterion the past earnings of any period, whether depressed or prosperous. It looked to prospective earning capacity for the long-term future. For an intelligent appraisal of that determinant, it had before it, and considered (as its Reports show), information on every factor significantly affecting the road's chances for obtaining and handling any particular physical volume of business in the future and for translating that service into net earnings available for return to security holders. For example it weighed, with obvious care, voluminous evidence on past and present trends of traffic (including the development of new sources of traffic in wartime), the large improvements that have been made to the property and the trend of unit costs of operation as affected by those improvements and by other developments of an apparently secular character.\* In short, the record of past earnings was only one of the factors surveyed in this broader setting as clues to the probable range of future earnings experience.

There is, accordingly, no basis for an argument that the Commission founded its action only on the record of past earnings. There is still less basis for the argument, which is the main premise of the Missouri Pacific Petition, that the earnings so used were those of depression years alone. The facts on their face preclude any such contention for the approved capitalization is so large that a fair return on the new securities would not be provided by the earnings of the past, looking for this purpose not to depression years, but to the average earnings of all the years, good and bad, in the last quarter of a century.

Annual requirements under the Plan through dividends on the Preferred Stock on all securities to be publicly held or

---

\* E. g., Submission Pamphlet 42-48, 66-69, 82-85, 118-121, 122-125, 156-159.

pledged under the new notes are \$4,487,015.\* This rises to a total of \$6,649,449 if dividends are included on the new common stock at 5%. Historical earnings, however, for the whole period 1921-1944 are substantially less than this total. After Federal income taxes at an assumed rate of 35%, the average annual earnings for that period are only \$4,647,000.\*\* After Federal income taxes as reported in those years, the corresponding figure is \$5,314,000.† The "depression" earnings of 1932-1935, considered by the Commission on the point of permissible new fixed charges, which, in contrast to dividends on stock, must be earned under the *most adverse* conditions reasonably foreseeable, were \$3,600,000. Clearly, therefore, the Commission could not have given decisive effect to depression earnings in its determination of the total permissible new capitalization, but must have given substantial weight to the prosperous years before the depression and the extraordinary war years that have followed it. Indeed, the total new capitalization is so large that nothing at all was earned for the new common stock in any year of that whole period except in the peak prosperity years of 1925-1930 and the extraordinary war years of 1942-1944.

---

\* This does not include equipment trust interest or interest on new securities originally provided for an issue (the Junction Bonds) since acquired by the estate.

\*\* Computed from annual statements of record (Tr. III 19-348 and 547). Minor accounting adjustments required by the Commission are reflected. The income tax rate is taken merely as an illustration and is applied as if the Plan had been in effect throughout the total period. Earnings through 1942 (the year of greatest net earnings in all history) were before the Commission; those of 1943-1944 are in the present record and are included in the calculation.

† Federal income taxes actually reported in the past are, of course, an inadequate measure of the future burden because (i) pre-war rates were lower than probable rates for the long-term post-war future, and (ii) the road was shielded from their impact by the deductions available under its excessive debt capitalization, which is now to be ended.

There has been no materially advantageous change of conditions since the Commission acted. On the contrary, the largest Gross Income\* of the Debtor in all history was before the Commission when it acted and was referred to in its report.\*\* Since then Gross Income has drastically declined. While this was in large part due to an increase in income taxes, it is also true that the sum of Gross Income and the amount deducted for income taxes has been progressively less in spite of large war-time increases in Railway Operating Revenues.† This reflects an apparently inexorable continuation of the rising trend in unit costs of operation that has characterized the position of the railroads for a number of years. Thus despite \$15,000,000 more Railway Operating Revenues in 1943, the balance carried down to Gross Income and income taxes was less. Railway Operating Revenues in 1944 were at the 1943 level, but further increases in operating costs left \$3,000,000 less for Gross Income and income taxes.

\* Total Railway Operating Revenues less railway operating expenses and taxes (including income taxes) plus or minus the net balance of payments for hire of equipment and joint facilities produce net railway operating income. Adding other income, we get Gross Income. Deducting miscellaneous deductions from income, we get income available for fixed charges (or "available for interest" if, as in the case of the Debtor, the miscellaneous deductions include rent for leased road and interest on unfunded debt). The text uses Gross Income rather than the last account to avoid a distortion (disadvantageous to the Stockholder Petitions) otherwise arising from a special charge among miscellaneous deductions in 1944.

\*\* Pages 158-9 of Submission Pamphlet.

† These are the reported figures in ('000's) :

	1942	1943	1944
Gross Income .....	\$17,444	\$12,305	\$10,912
Income taxes .....	2,180	7,184	5,338
Total .....	19,624	19,489	16,250
Ry. Operating Rev. ....	54,475	70,194	70,347

Source : Tr. II 353 and Tr. III p. 547.



If operating results show such a pattern with the unprecedented volume of business carried in war years, surely the Commission was entitled to its apprehensions for the post-war future that has now begun, when the Debtor's traffic can no longer be sustained at such levels by the wholly extraordinary, and it is hoped non-recurring, conditions of the war in the Pacific.

So in this case the change of conditions since the Commission's action has been adverse. But even were it favorable, the Court has made it clear that "the bulge of war earnings" is not to be allowed to upset Commission plans (*Milwaukee Case* above at p. 543-4; *Western Pacific Case* above at pp. 508-9; see also *I. C. C. v. Jersey City*, 322 U. S. 503, 1944).

It is therefore beyond the reach of argument that the Commission had before it an adequate and representative record and applied proper standards in determining the total permissible new capitalization. Indeed, in doing so, it went farther, and permitted a relatively larger new capitalization than is its general practice.\*

It may also be pertinent to note, for the interest of the asserted issues is not unrelated to the position of him who asserts them, that the new securities (even when taken at their face amount) fall far short of covering the total claim of creditors. Most conspicuously, the General Mortgage bondholders, for their total claim of nearly \$44,000,000,

---

\* The new capitalization in this case is larger than in the average of all other important railroad cases, whether viewed in relation to the largest earnings in any year of the decade 1930-1939 or in relation to the physical values found by the Commission. The facts from which this purely mathematical calculation has been made appear in the published reports of the Commission and may be judicially noticed. The trial court, with its large administrative experience with the property, was troubled on this score, saying "... it is very doubtful in my mind if the new capital structure is not too large" (Tr. II 467).

receive only 10% in new common stock taken at its par value, leaving 90% of their claim unrecognized. All of that would, of course, have to be satisfied in full before anything of value could be found for junior interests. There is no possibility of such miracles.

We submit, therefore, that Questions 1 and 2 in the Missouri Pacific Petition (whether the Commission may "give effect only to past earnings" in "years of . . . depression") are not presented by the record.

Question 3 in the Missouri Pacific Petition (whether old stock may be excluded despite "a reasonable probability" of earnings in prosperous years adequate to permit "substantial dividends") is also not presented by the record, for there is no such "reasonable probability." On the contrary, the new common stock given to senior bondholders is so far removed from earnings that, after Federal income taxes at 35%, common dividends at 5% have never been earned except in the extraordinary war years of 1942-1944; indeed the balance of earnings after such dividends for the whole period 1921-1944 was a deficit of nearly \$60,000,000.\* When a representative average is inadequate for a fair return, the top earnings of peak years included in the average are not available for any junior interests. Particularly not for the old stock championed by the Missouri Pacific Petition, for all of it is separated from these earnings by the \$40,000,000 vacuum of the unsatisfied General Mortgage

---

\* The computation is the same as that referred to in note \*\* on page 4 above. The elimination of all Federal income taxes would still leave a cumulative deficit (of about \$26,000,000) and would add only three other years when 5% common dividends would have been covered—1926 when the remainder of earnings would have been \$700,000, and 1928, \$220,000, and 1929, \$1,800,000. The old stock is not entitled to compute earnings on the basis of the old capitalization with its heavy debt structure which the road could not support in the past and the public interest can not tolerate in the future.

claim. We say, therefore, that there is no reasonable probability of earnings available for dividends on the old stock in any years, but on the contrary an evident exclusion of any such probability.

The Missouri Pacific Petition is thus no more than an appeal for a new exercise of administrative judgment, on the ground that, within the area of permissible administrative judgment, the new capitalization might have been, and should have been, fixed at a substantially greater amount than the Plan provides.

This is not a justiciable question and, if it were, it would be merely a question of the proper appraisal of the earnings prospects of this particular road. That is not a question of any general interest. The Petition should, therefore, be denied, as was the analogous petition in *Chicago and North Western R. v. Mutual Savings Bank Group Committee*, 318 U. S. 793 (1943).

Such arguments are at bottom mere requests for re-examination of the facts. This Court has repeatedly refused to re-examine findings of fact approved both by a District Court and by a Circuit Court (*v. Tennessee Coal, Iron & Railroad Co. v. Muscoda Local*, 321 U. S. 590, 605, conc. op., 1944) and administrative findings approved by a Circuit Court (*National Licorice Co. v. N. L. R. B.*, 309 U. S. 350, 357, 1940). On the decisive point of the Stockholder Petitions all three tribunals have concurred.

## C

## CONCLUSION

The Stockholder Petitions raise no question of general interest, and, indeed, raise no arguable question of any kind.

We respectfully submit that they should be denied.

Dated September 8, 1945.

HAROLD JUDSON

*Acting Solicitor General*

W. MEADE FLETCHER, JR.,  
811 Vermont Avenue, N. W.,  
Washington 25, D. C.  
*For Reconstruction Finance Corporation*

HUNTON, WILLIAMS, ANDERSON, GAY & MOORE  
1003 Electric Building  
Richmond 12, Virginia

HENRY W. ANDERSON

GEORGE D. GIBSON

1003 Electric Building  
Richmond 12, Virginia  
*For Insurance Group Committee*

RATHBONE, PERRY, KELLEY & DRYE  
70 Broadway  
New York 4, N. Y.

ALEXANDER M. LEWIS

70 Broadway  
New York 4, N. Y.  
*For Central Hanover Bank and Trust Company, Trustee, Rio Grande Western Railroad Company First Trust Mortgage*

DAVIS POLK WARDWELL SUNDERLAND & KIENDL  
15 Broad Street  
New York 5, N. Y.

JOHN W. DAVIS

EDWIN S. S. SUNDERLAND

JAMES L. HOMIRE

THOMAS O'G. FITZGIBBON

JUDSON C. MCLESTER, JR.

15 Broad Street  
New York 5, N. Y.  
*For Guaranty Trust Company of New York, Trustee, Rio Grande Western Railroad Company Consolidated Mortgage*

STEWART & SHEARER  
45 Wall Street  
New York 5, N. Y.

W. A. W. STEWART

45 Wall Street  
New York 5, N. Y.

*For United States Trust Company of New York, Trustee, Denver and Rio Grande Railroad Company Consolidated Mortgage*

MILBANK, TWEED & HOPE  
15 Broad Street  
New York 5, N. Y.

ARTHUR A. GAMMELL

15 Broad Street  
New York 5, N. Y.

*For The Chase National Bank of the City of New York, Trustee, Denver and Rio Grande Western Railroad Company Refunding and Improvement Mortgage*